Mistaria Sdn Bhd v Evergreen Furniture Industries Sdn Bhd

HIGH COURT (KUALA LUMPUR) — SUIT NO S2-22-127 OF 1998
KAMALANATHAN RATNAM J
21 MAY 1999

Contract *— Consideration — Total failure of — Sale of business — Consideration to flow from third party — Purchase consideration not paid — Burden to make payment on third party — Whether plaintiff as vendor can enjoy fruits flowing from sale of business — Whether defendant can be said to have parted with its business*

The plaintiff contends that a shareholders' agreement dated 5 November 1996 was entered between the plaintiff and the defendant ('the agreement'). In the agreement, both parties had agreed to set up another company named Evergreen United Industries Sdn Bhd ('EUI') to take over the business and assets of the defendant. The plaintiff alleges that EUI has bought over from the defendant its goodwill and all existing orders and contracts at the nominal sum of RM1 only. The plaintiff alleges that the defendant had breached the terms of the agreement by continuing to issue out invoices and to collect monies due from its debtors up to a sum of RM4,125,669.49. The plaintiff is now seeking a declaration that the defendant is indebted to EUI for the sum of RM4,125,669.49 which the defendant had collected from its debtors. It is also seeking a declaration that the uncollected balance of RM1,463,829.70 due to the defendant is a debt owing to EUI, together with various other related orders. Judgment in default of defence pursuant to O 19 r 7(1) was given on 18 May 1998. The defendant applied to set aside the judgment. The defendant submitted that there had been a failure on the part of EUI to pay the purchase consideration. The plaintiff argued that the consideration was not due from the plaintiff but was due from EUI.

Held, allowing the application:

The defendant has successfully shown that it has a bona fide reasonable defence as there had been a complete failure of consideration of the shareholders' agreement which is actually a sale and purchase agreement of the defendant's business and a shareholders' agreement rolled into one agreement.

Before the agreement can be completed, certain consideration must flow from EUI to the defendant. To enable EUI to obtain that consideration, it had been provided in the agreement that the plaintiff who is a 70% shareholder of EUI has to obtain the RM2m financing and the RM500,000 leasing facilities. If the purchase consideration had not been paid, even though the burden is on EUI to make the payment, the plaintiff cannot enjoy the fruits flowing from the arrangement, much less can the plaintiff on behalf of EUI seek a declaration that the defendant is indebted to EUI. A fundamental

requirement has not been fulfilled by EUI and hence the defendant cannot be said to have parted with its business (see pp 104C–D, 103H–104B). A

[**Bahasa Malaysia summary**

Plaintif menegaskan bahawa perjanjian pemegang saham bertarikh 5 November 1996 telah dimasuki antara plaintif dan defendan ('perjanjian tersebut'). Di dalam perjanjian tersebut, kedua-dua pihak telah bersetuju untuk menubuhkan suatu syarikat lain dengan nama Evergreeen United Industries Sdn Bhd ('EUI') untuk mengambilalih perniagaan dan aset-aset defendan. Plaintif mendakwa bahawa EUI telah menbeli daripada defendan nama baik dan semua pesanan dan kontrak-kontrak yang wujud pada kadar nominal RM1 sahaja. Plaintif mendakwa bahawa defendan telah melanggar terma-terma perjanjian tersebut dengan meneruskan pengeluaran invois-invois dan mengutip hutang tertunggak daripada penghutang sehingga berjumlah sebanyak RM4,125,669.49. Plaintif sekarang memohon suatu deklarasi bahawa defendan terhutang kepada EUI sejumlah RM4,125,669.49 di mana defendan telah memperolehi daripada penghutang. Ia juga memohon suatu deklarasi bahawa baki jumlah RM1,463,829.70 yang tertunggak kepada defendan adalah hutang yang tertunggak kepada EUI, bersama dengan pelbagai perintah lain yang berkaitan. Penghakiman ingkar terhadap pembelaan menurut A 19 k 7(1) telah diberikan pada 18 Mei 1998. Defendan telah memohon unutk mengenepikan penghakiman tersebut. Defendan menghujahkan bahawa terdapat kegagalan di pihak EUI untuk membayar balasan pembelian tersebut. Plaintif telah mempertikaikan bahawa balasan tersebut bukanlah patut datang daripada plaintif tetapi daripada EUI. B C D E F

Diputuskan, membenarkan permohonan tersebut:

Defendan telah berjaya untuk menunjukkan bahawa wujud pembelaan munasabah bona fide kerana terdapat kegagalan yang nyata terhadap balasan kepada perjanjian pemegang saham yang sebenarnya adalah merupakan suatu perjanjian jual beli syarikat defendan dan perjanjian pemegang saham yang disatukan ke dalam satu perjanjian. G

Sebelum perjanjian ini boleh diselesaikan, balasan tertentu mesti datang daripada EUI kepada defendan. Untuk membolehkan EUI memperolehi balasan tersebut, adalah diperuntukkan di dalam perjanjian tersebut bahawa plaintif, yang merupakan pemegang saham 70% EUI, perlu memperolehi pembiayaan RM2 juta itu dan kemudahan pajakan RM500,000 itu. Jika balasan pembelian tersebut belum dibayar lagi, walaupun beban adalah pada EUI untuk membuat bayaran tersebut, plaintif tidaklah boleh menikmati pulangan dari pakatan tersebut, apatah lagi plaintif bagi pihak EUI memohon suatu deklarasi bahawa defendan terhutang kepada EUI. H I

Suatu keperluan asas telah tidak dipenuhi oleh EUI dan oleh demikian defendan tidak boleh dikatakan telah terpisah dengan perniagaannya (lihat ms 104C–D, 103H–104B).]

Notes

For cases on total failure of consideration, see 3 *Mallal's Digest* (4th Ed, 1997 Reissue) paras 1879–1881.

Cases referred to

Hasil Bumi Perumahan Sdn Bhd & Ors v United Malayan Banking Corp Bhd [1994] 1 MLJ 312 (refd)

Legislation referred to

Rules of the High Court 1980, O 19 r 7(1)

Lim Bee Leong (*Dorairaj Low & Teh*) for the plaintiff.
D Kalai (*Kalai & Partners*) for the defendant.

Cur Adv Vult

Kamalanathan Ratnam J: This is an application to set aside a judgment dated 18 May 1998. The judgment was obtained by the plaintiff pursuant to O 19 r 7(1) of the Rules of the High Court ('RHC') made by way of a summons in chambers dated 29 April 1998 (encl 9). Order 19 r 7(1) of the RHC reads as follows:

> Default of defence: Other claims
>
> (1) Where the plaintiff makes against a defendant or defendants a claim of a description not mentioned in r 2 to 5, then, if the defendant or all the defendants (where there is more than one) fails or fail to serve a defence on the plaintiff, the plaintiff may, after the expiration of the period fixed by or under these rules for service of the defence, apply to the court for judgment, and on hearing of the application the court shall give such judgment as the plaintiff appears entitled to on his statement of claim.

In its affidavit in support of encl 9 affirmed on 27 April 1998, the plaintiff's solicitors deposed that the amended writ and statement of claim had been served on the defendant on 2 April 1998 and that to date, no appearance had been entered on behalf of the defendant. The plaintiff had also on 5 March 1998 obtained an ex parte injunction restraining the defendant, its agent or servant from receiving any payments from its debtors until after the hearing of its inter partes application for a mandatory injunction.

The basis of the plaintiff's claim against the defendant as stated in its statement of claim is that there was a shareholders' agreement dated 5 November 1996 between the plaintiff and the defendant ('shareholders' agreement'). In that shareholders' agreement the plaintiff alleges that both parties had agreed to set up another company named Evergreen United Industries Sdn Bhd ('EUI') to take over the business and assets of the

defendant. The plaintiff further alleges that EUI has bought over from the defendant its goodwill and all existing orders and contracts at the nominal sum of RM1 only. Further, at paras 6 and 7 of its statement of claim, the plaintiff alleges that the defendant had, in breach of the terms of the shareholders' agreement, continued to issue out invoices and to collect monies due from its debtors up to a sum of RM4,125,669.49. The plaintiff is now seeking a declaration from this court that the defendant is indebted to EUI for the sum of RM4,125,669.49 which the defendant had collected from its debtors. It is also seeking a declaration that the uncollected balance of RM1,463,829.70 due to the defendant is a debt owing to EUI, together with various other related orders. The plaintiff completely left out of its pleading the other two relevant sub-clauses in the shareholders' agreement. Clause 3(v) of the shareholders' agreement states as follows:

> The purchase by the Company (EUI) from EFI (defendant) of its —
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> (a) fixed assets as shown in the Schedule hereto annexed at the price of RM2m;
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> (b) its stock-in-trade valued at RM865,256; and
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> (c) goodwill and all existing orders and contracts at the nominal sum of Ringgit One (RM1) only.

The purchase price of the fixed assets shall be paid over a period of sixty (60) months by equal monthly instalments, the first to commence one (1) month after the date of execution of this agreement. The stock-in-trade shall be purchased subject to written confirmation of acceptance by the company (EUI) of stocks upon each transfer as and when requested by the company (EUI).

The defendant's marketing director had in her affidavit affirmed on 13 November 1998 stated that there was another company, that is, Falcrest Pte Ltd ('FPL'), that had entered into an agreement with the defendant to purchase the defendant company. She exhibited an agreement dated 1 March 1996 (the 1 March 1996 agreement) to support her averment. She alleges that one Hu Chang Pee owned FPL and that the same Hu Chang Pee is a director of the plaintiff. She further avers that on 16 October 1996, the paid-up capital of EUI was increased to RM100,000 and that FPL had requested the defendant to transfer its 70% shares to the plaintiff, which the defendant agreed to. The defendant further avers in cll 17 and 18 that the monies due from FPL under cl 3(vi) of the 1 March 1996 agreement had been outstanding and remains unpaid although she and the defendant had made numerous demands for the payment. The payment term in cl 3(vi) of the 1 March 1996 agreement is similar to that in cl 3(v) of the shareholders' agreement except that the date of commencement of the payment is different. The date of commencement of payment of the purchase price is stated as follows:

> The purchase price of the fixed assets and stock-in-trade shall be paid over a period of sixty (60) months by equal monthly instalments the first to commence six (6) months after commencement of business by the Company (EUI).

A The plaintiff, by way of Hu Chang Pee's affidavit affirmed on 5 December 1998, denied the defendant's allegation. The plaintiff, however, did not state with specific details nor did it state at all that the monies due under the shareholders' agreement or the 1 March 1996 agreement had been paid to the defendant. The plaintiff had been less than candid in its pleadings by not pleading the whole clause as it existed in the agreements but had only B relied on cl 3(v)(c), thus presenting an incomplete picture to the court. Even when confronted with a positive averment of not having made the payments due in Cl 3 (v)(a) and (b), the plaintiff just put up a mere denial. Even the payment of RM1 under cl 3(v)(c) had not been shown to have been made.

C The plaintiff's submission is that the monies are due from EUI and not the plaintiff or FPL and that the failure to plead that such obligation has been fulfilled will not defeat the plaintiff's claim as it never was the plaintiff's obligation to make any payment.

From the shareholders' agreement I can discern upon whom that responsibility lies. Clause 9, referring to loan and finance, is very telling, D particularly at cll 9.1 and 9.3 where it is provided as follows:

> 9.1 Arrangement of banking facilities
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> As agreed between the parties hereto MSB has sourced and arranged for banking facilities ('the Said Facilities') of Ringgit Two Million (RM2m) for the Company's (EUI) working capital to finance the Business.
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> E 9.2 Provision of Security by MSB
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> (a) ...
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> (b) ...
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> (c) ...
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> F 9.3 Arrangement of further facilities
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> MSB has also agreed that it will assist the Company (EUI) to arrange further facilities for its use and pursuant thereto MSB has successfully arranged for a leasing or hire-purchase company to provide leasing or hire-purchase facilities to the Company (EUI) in the sum of Ringgit Five Hundred Thousand (RM500,000) upon such terms and conditions as may be agreed to between the leasing or hire-purchase company and the G Company (EUI).

The payment of RM100,000 as the paid-up capital of EUI was only to enable the plaintiff and FPL to set up EUI which was the vehicle agreed upon by the parties to acquire the defendant. It did not immediately entitle the plaintiff to the assets of the defendant. It merely means that EUI is now H in a position to commence whatever business it has decided to undertake, which in this case is to take over the business of the defendant, as envisaged by the shareholders' agreement. However, before the agreement can be completed, certain consideration must flow from EUI to the defendant. To enable EUI to obtain that consideration, it had been provided in the agreement that the plaintiff who is a 70% shareholder of EUI has to do I certain things, the major ones being to obtain the RM2,000,000 financing and the RM500,000 leasing facilities. The defendant says that there had been a failure on the part of EUI to pay the purchase consideration and the

plaintiff says that that is none of its business as the consideration is not due from the plaintiff but is due from EUI. My view is that if the purchase consideration had not been paid, even though the burden is on EUI to make the payment, the plaintiff cannot enjoy the fruits flowing from the arrangement, much less can the plaintiff on behalf of EUI seek a declaration that the defendant is indebted to EUI. The plaintiff has to make the payment happen first by obtaining the money for EUI to pay to the defendant, that being its obligation under cl 9. A fundamental requirement has not been fulfilled by EUI and hence the defendant cannot be said to have parted with its business as not a single sen has been paid and that the business now belongs to EUI and the plaintiff being a 70% shareholder of EUI can now partake of its fruits.

The plaintiff has chosen not to address the court on any of the payment or failure of consideration issues raised by the defendant in its affidavits on its submissions except to say that it is not its obligation to pay. The defendant has successfully shown that it has a bona fide reasonable defence as there had been a complete failure of consideration of the shareholders' agreement which is actually a sale and purchase agreement of the defendant's business and a Shareholders' Agreement rolled into one agreement. Therefore, the court ought to set aside the judgment dated 18 May 1998 as the defendant has 'a good defence which has merits and to which the court should pay heed' to. The defendant, to quote the words of the Supreme Court in *Hasil Bumi Perumahan Sdn Bhd & Ors v United Malayan Banking Corp Bhd* [1994] 1 MLJ 312 at p 321 has shown that:

> ... his defence is not a sham defence but one that is prima facie, raising serious issues as a bona fide reasonable defence that ought to be tried ... .

Accordingly, I allow the defendant's application to set aside the judgment dated 18 May 1998 with costs. The defendant is to file and serve its defence on or before 4 June 1999. I wish to remind counsel for the defendant that he is to take the necessary steps within the time periods set by the RHC or the court or face the consequences of his documents being rejected by the court or worse still, judgment being entered against his client.

Defendant's application allowed.

Reported by Benjamin Yong